

**ST 02-4**

**Tax Type: Sales Tax**

**Issue: Machinery & Equipment Exemption – Manufacturing**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
SPRINGFIELD, ILLINOIS**

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<b>THE DEPARTMENT OF REVENUE</b>	)	<b>Docket #</b>	<b>99-ST-0000</b>
<b>OF THE STATE OF ILLINOIS</b>	)		
	)	<b>IBT #</b>	<b>0000-0000</b>
<b>v.</b>	)	<b>NTL #</b>	
	)		
<b>ABC CORPORATION</b>	)		
<b>Taxpayer</b>	)	<b>Barbara S. Rowe</b>	
	)	<b>Administrative Law Judge</b>	

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**RECOMMENDATION FOR DISPOSITION**

Appearances: Natasha Bukorovic, Law Office of George S. Brasovan for ABC Corporation; Mr. James Day and Mr. Charles Hickman, Special Assistant Attorneys General for the Illinois Department of Revenue.

**Synopsis:**

This matter involves two Notices of Tax Liability issued by the Illinois Department of Revenue (hereinafter referred to as the "Department") to ABC Corporation (hereinafter referred to as the "Taxpayer") for the period of December 1, 1990 through July 31, 1996. ABC Corporation timely protested the notices. An evidentiary hearing was held during which the taxpayer argued that the transactions involving XZY Steel were exempt under the manufacturer's machinery and equipment exemption of the Service Use Tax Act/Use Tax Act. After a thorough review of the facts and law presented, it is my recommendation that the assessments for the transactions with XXX Company be cancelled; the assessments for transactions that occurred prior to July 1, 1991, be cancelled; and the remainder of the assessments be upheld. In support thereof, I make the following findings and conclusions in accordance with the requirements of Section 100/10-50 of the Administrative Procedure Act (5 ILCS 100/10-50).

## **FINDINGS OF FACT:**

1. The *prima facie* case of the Department was established by the admission into evidence of the Notices of Tax Liability 00 0000000000000000 and 00 0000000000000000 as State's. Ex. Nos. 1 & 2. (Tr. p. 11)

2. On December 24, 1998, the Department issued to the taxpayer Notice of Tax Liability 00 0000000000000000 for Service Use Tax/Use Tax due on purchases for the period of July 1, 1990 through November 30, 1993 in the tax amount of \$74,497.00; penalty of \$22,349.00; and interest of \$51,151.00, for a total liability of \$147,997.00. (State's Ex. No. 2)

3. On December 24, 1998, the Department issued the taxpayer Notice of Tax Liability 00 0000000000000000 for Service Use Tax/Use Tax due on purchases for the period of December 1, 1993 through July 31, 1996 in the tax amount of \$58,189.00; penalty of \$2,473.00; and interest of \$19,464.00, for a total liability of \$80,126.00. (State's Ex. No. 1)

4. The taxpayer is located at 1234 Anywhere Street in Somewhere, Indiana. The taxpayer was not registered with the Department for Retailers' Occupation or related tax collection prior to the audit conducted by the Department. The taxpayer is an out-of-state de-minimus service establishment. The taxpayer provides heating and air conditioning services to Illinois customers. In conjunction with the taxpayer's services, certain items of tangible personal property are transferred to the taxpayer's customers. The Department determined that the taxpayer has a service use tax collection obligation to the State of Illinois. (Tr. pp. 5-6, 16)

5. The majority of the transactions identified are with XXX Company, the major customer of the taxpayer. The Department concedes that XXX Company paid the service use tax attributable to the transactions between it and the taxpayer. (Tr. p. 6)

7. The taxpayer submitted an unexecuted "Blanket Sales Tax Exemption Certificate" from XZY Steele Company. (Taxpayer's Ex. No. 1)

8. The waivers of the statute of limitations executed by the taxpayer with the Department did not cover the initial part of the audit period, specifically July 1, 1990 through July 1, 1991. (State's Group Ex. No. 4)

9. The auditor examined a 36-month period within the audit period, arrived at the liability for that period, and projected those numbers over the 73-month period at issue. (State's Ex. No. 3; Tr. p. 10)

10. ABC Corporation ceased doing business on January 1, 1996. (Tr. p. 15)

### **CONCLUSIONS OF LAW:**

The Service Use Tax Act imposes a tax on the privilege of using in Illinois real or tangible personal property acquired as an incident to the purchase of a service from a serviceman, \* \* \* 35 ILCS 110/3.

The three issues to be addressed in this recommendation are:

- (1) whether taxpayer's transactions with XXX Company assessed by the Department are taxable to the taxpayer;
- (2) whether the liability for the remaining transactions, mainly with XZY Steele, are exempt pursuant to the manufacturer's machinery and equipment exemptions under the Service Use Tax Act and the Use Tax Act; and
- (3) whether the statute of limitations bars liability for the assessments for the period of July 1, 1990 through July 1, 1991.

The Department concedes that XXX Company has paid the service use tax attributable to the transactions between the taxpayer and XXX Company. Therefore, those portions of the assessments are cancelled. The Department also concedes that no waiver of the statute of limitations was received for the period of July 1, 1990 through July 1, 1991. Therefore, the assessments for that period are cancelled.

The only remaining issue is whether the taxpayer is legally responsible for the liability for the remainder of the transactions still at issue, mainly with XZY Steele.

The taxpayer argues that the manufacturing and machinery exemption set forth at §2(5) of the Service Use Tax Act (hereinafter referred to as "SUTA") found at 35 **ILCS** 110/2(5) and §3-50 of the Use Tax Act (hereinafter referred to as the "UTA") found at 35 **ILCS** 105/3-50 is applicable to the transactions with XZY Steel.

The relevant portion of the statutes at 35 **ILCS** 110/2 states:

"Sales of service means any transaction except: \* \* \*

(5) a sale or transfer of machinery and equipment used primarily in the process of the manufacturing or assembling, either in an existing, an expanded or a new manufacturing facility, of tangible personal property for wholesale or retail sale or lease, whether such sale or lease is made directly by the manufacturer or by some other person, whether the materials used in the process are owned by the manufacturer or some other person, or whether such sale or lease is made apart from or as an incident to the seller's engaging in a service occupation and the applicable tax is a Service Use Tax or Service Occupation Tax, rather than Use Tax or Retailers' Occupation Tax.

\* \* \*

Exemption (5) also includes machinery and equipment used in the general maintenance or repair of such exempt machinery and equipment or for in-house manufacture of exempt machinery and equipment. For the purposes of exemption (5), each of these terms shall have the following meanings: (1) "manufacturing process" shall mean the production of any article of tangible personal property, whether such article is finished product or an article for use in the process of manufacturing or assembling a different article of tangible personal property, by procedures commonly regarded as manufacturing, processing, fabricating, or refining which changes some existing material or materials into a material with a different form, use or name.

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(3) "machinery" shall mean major mechanical machines or major components of such machines contributing to a manufacturing or assembling process; and (4) "equipment" shall include any independent device or tool separate from any machinery but essential to an integrated manufacturing or assembly process; \* \* \* The purchaser of such machinery and equipment who has an active resale registration number shall furnish such number to the seller at the time of purchase. The user of such machinery and equipment and tools without an active resale registration number shall prepare a certificate of exemption for each transaction stating facts establishing the

exemption for that transaction, which certificate shall be available to the Department for inspection or audit. \* \* \* (emphasis added)

The UTA contains identical language at 35 **ILCS** 105/3-50.

The taxpayer has presented no evidence that a certificate of exemption for each transaction, stating facts that establish the exemption for that transaction, were provided as required by the statute. An unexecuted "Blanket Sales Tax Exemption Certificate" from XZY Steel Company does not satisfy the statutory requirement.

The taxpayer relies on City Suburban Electric Motors, Inc. v. Wagner, 278 Ill.App.3d 564 (1<sup>st</sup> Dist. 1996) for support of the proposition that the materials and machinery provided by the taxpayer fall within the statutory definition of exempt equipment involved in the general maintenance and repair of exempt equipment. The taxpayer is correct that general maintenance and repair of exempt equipment may qualify for the exemption; however, that does not negate the statutory requirement for the exemption certificate issued by user of the machinery and materials, for the purpose of relieving the vendor of the tangible personal property from establishing that the machinery is of an exempt nature.

It is well settled in Illinois that when a statute purports to grant an exemption from taxation, the tax exemption provision is to be construed strictly against the one who asserts the claim of exemption. Thomas M. Madden and Co. v. Department of Revenue, 272 Ill.App.3d 212 (2nd Dist. 1995) *rehearing denied*. Whenever doubt arises, it is to be resolved against exemption and in favor of taxation. Follett's Illinois Book & Supply Store, Inc. v. Issacs, 27 Ill.2d 600 (1963). A claimant must prove clearly and conclusively its entitlement to an exemption. Wyndemere Retirement Community v. Department of Revenue, 274 Ill.App.3d 455 (2<sup>nd</sup> Dist. 1995) *rehearing denied; leave to appeal denied* (164 Ill.2d 585). Further, in ascertaining whether or not a property is statutorily tax exempt, the burden of establishing the right to the exemption is on the one who claims the exemption. Midway Airlines, Inc. v. Department of Revenue, 234 Ill.App.3d 866 (1<sup>st</sup> Dist. 1992) *leave to appeal denied* (146 Ill.2d 632) The

taxpayer failed to supply the required certificates and therefore failed to provide legally sufficient evidence that the tangible personal property it sold was exempt from the pertinent tax.

For the foregoing reasons, it is recommended that the portion of the liability at issue attributable to the taxpayer's transactions with XXX Company be cancelled and the portion of the liability for the period of July 1, 1990 through July 1, 1991 also be cancelled. It is further recommended that the remainder of the liability be upheld.

Respectfully Submitted:

Date: January 2, 2002

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Barbara S. Rowe  
Administrative Law Judge